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IN THE

Supreme Court of the United States

October Term, 1954.

No. 292.

THE FIRST TRUST AND SAVINGS BANK OF ZANESVILLE, OHIO,

Petitioner,

v.

FIDELITY-PHILADELPHIA TRUST COMPANY.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

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FIDELITY-PHILADELPHIA TRUST COMPANY.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

The petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, entered in this case on June 28, 1954.

OPINIONS BELOW.

The opinion of the District Court (R 205a-228a) is reported in 112 F. Supp. 761.[1] The opinion of the Court of Appeals, printed in the Appendix, was not reported officially at the time of the preparation of this petition.

1. An earlier memorandum opinion in this case and in ten similar cases on defendant's motions for a more definite statement and to strike the complaint is reported in 12 F. R. D. 195.

JURISDICTION.

The judgment of the Court of Appeals was entered on June 28, 1954. A petition for rehearing was denied on July 20, 1954. The jurisdiction of this Court is invoked under 28 U. S. C. § 1254(1).

QUESTIONS PRESENTED.

Is § 12(2) of the Securities Act of 1933 inapplicable to a bank on the ground that it is an agent and not a seller, within the meaning of the Act, when it made and mailed misleading and untrue statements to purchasers in the course of its disposition of collateral notes which were deposited with it by its customer for an immediate loan and for the collection of the purchase price?

Can a defendant avoid the statutory liability under the Securities Act for misleading and untrue statements on the ground that it gave a warning or that it had no common law duty to investigate the truth?

STATUTE INVOLVED.

Section 12(2) of the Securities Act of 1933, as amended, 15 U. S. C. § 771 (2) reads as follows:

"Any person who—

* * *

> sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

§ 2(3) of the Act defines "sell" as follows:

> "(3) the term 'sale', 'sell', 'offer to sell', or 'offer for sale' shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value; except that such terms shall not include preliminary negotiations or agreements between an issuer and any underwriter. . . ."

STATEMENT.

A. History of the Litigation.

The present action, in addition to ten other actions,[2] was filed in the United States District Court for the Eastern District of Pennsylvania in order to obtain restitution for losses which followed untrue and misleading statements made and mailed by the defendant. The losses stemmed from the purchase by the plaintiffs of notes which were secured by documents fraudulently printed by the president of a customer of the defendant, and retained in the custody of the defendant. Relief was sought under the Securities Act, as well as under the common law. Federal jurisdiction was based upon § 22(a) of the Securities Act, 15 U. S. C. § 77 v(a). It was also based upon diversity of citizenship in this case and in several of the remaining ten cases.

This case, the first one of the eleven cases filed, was tried without a jury in January of 1953. Judgment was entered in favor of the defendant on May 28, 1953. Plaintiff's motions to amend the findings and the judgment, and for a new trial, were filed on June 5, 1953 and were denied on November 2, 1953. An appeal was filed on November 30, 1953. It was argued on April 6, 1954, and judgment was affirmed on June 28, 1954.

The District Judge and the Court of Appeals both held that the defendant was not a seller within the meaning of the Securities Act. The Court of Appeals also concluded

2. The plaintiffs in the other ten actions are: Merchants National Bank of Quakertown; Oil City Trust Company; The New Haven Bank, N. B. A.; Oil City National Bank; The Bristol Trust Company; Jefferson-Gravois Bank; The Second National Bank of New Haven; First National Bank in Birdsboro; Western Bank, 130 East First Street, Long Beach, California; and the First National Bank, Philipsburg, Pennsylvania. The amount of the claims involved in all eleven actions exceeds $875,000.00.

that if the Act were applicable, there was no liability: (1) for the misleading statement because it was cured by another part of the statement which the court below deemed a warning; and (2) for the untrue statement because the defendant was deemed to be under no duty to investigate the correctness of its statement that it had warehouse receipts of the named distillery. Both courts below concluded that there was no common law right of recovery.

The trial of each of the other ten cases has been kept in abeyance pending the final disposition of the legal questions in this case.

B. Material Facts Preceding the Litigation.

In March of 1938 (R 75a), the defendant began a system of issuing its receipts for collateral deposited by its customer, the Philadelphia Acceptance Corporation, hereinafter called PAC. The collateral was whiskey warehouse receipts. PAC was in the finance business and engaged in the purchase and sale of notes secured by these warehouse receipts. The notes were transferred to the defendant, on some occasions, for general loans on its own account and, on other occasions, for temporary loans in connection with the collection thereon by the defendant from purchasing banks throughout the United States. In 1941 the plaintiff first accepted the plan of dealing with the receipts issued by the defendant for collateral which was delivered to the defendant by PAC and retained by the defendant (R 57a).

In 1947 the sole owner and president of PAC was Charles W. Collom. He was very friendly with one vice-president of the defendant who handled PAC's account (R 89a) and had a joint business interest with another vice-president who participated in the handling of PAC's account (R 146a, 155a, 159a).

In 1947 Collom forged a large number of warehouse receipts of the Carrollton Springs Pure Rye Distillery, Inc.,

and the defendant for approximately three years thereafter dealt with these spurious warehouse receipts frequently on its own account in connection with substantial loans it granted to PAC (R 72a, 82a). It also made temporary loans on this spurious collateral which was deposited with it for the purpose of collecting on the sale of the collateral notes to approximately 45 banks in various parts of the country (R 76a-78a, 94a).

The plaintiff in 1949 wrote the defendant expressing concern about whether the collateral notes were high grade risks, and asking for an opinion as to the responsibility of PAC (R 38a). The defendant replied to that letter, making statements about PAC's bank balances and about the risk but failing to make any statement about PAC's overdrawals of its account and about a large judgment and substantial tax liens against Mr. Collom (R 39a).

The four specific claims involved in this case arose in 1950 out of the above background and under identical circumstances except for differences in dates and amounts. The first of these four transactions took place on July 5, 1950 when the plaintiff received two written communications, one from PAC and one from the defendant. PAC's letter stated that a new investment was being forwarded to replace a previous investment, and a so-called confirmation slip was enclosed. The defendant's letter included: (a) a draft drawn by PAC and endorsed by the defendant; (b) a transmittal slip; (c) a purported note which referred to the collateral; and (d) a receipt executed by the defendant stating that it had negotiable warehouse receipts of the Carrollton Springs Pure Rye Distillery, Inc. On the same day, after the receipt of these letters, the plaintiff mailed a check to the defendant for $19,000.

The other three transactions took place in the same month on the 18th, 20th and 24th, in the respective amounts of $24,000, $20,000 and $19,000. There is no real question as to any of the facts of all four transactions because, as

would be expected in banking transactions, there was documentary proof as to exactly what took place (R 67a).

In each of these four transactions, as well as in the great bulk of transactions with all the banks going back to 1948, the defendant extended credit to PAC and charged it interest as soon as the documents were delivered by PAC to the defendant (R 78a). Also, in each of the four transactions, there was the unqualified written statement of the defendant that it held warehouse receipts of the Carrollton Springs Pure Rye Distillery, Inc. (R 19a). Yet, in each of the transactions the purported warehouse receipts were spurious. The defendant admitted that no inquiry whatever had been made by it during the three-year period in which it had been handling the spurious warehouse receipts (R 71a, 72a).

REASONS FOR GRANTING THE WRIT.

1. The determination of whether a restricted interpretation should be given to the word "seller" under the Securities Act is an important question of federal law which has not been, but should be, settled by this Court. Great public significance also exists in the intertwined issue of whether banks, in the performance of banking operations, can be sellers within the meaning of the Act.

This Court has had the occasion to point out that "the protective provisions of the Securities Act require the exercise of judicial direction to fairly assure their effectiveness. . . ." *Wilko v. Swan,* 346 U. S. 427 (1953). Judicial supervision becomes particularly important when an inconclusive local statute is used to construe a defendant as an agent rather than as a disposer of collateral notes in order to set up an artificial discrimination to nullify a Congressional remedy.

The decisions of the courts below should not be permitted to interpret away the clear words of the Act. Their

conclusions should meet the same treatment given to the restricted interpretations of the Securities Act by the lower courts in *Securities & Exchange Commission v. Howey Company*, 328 U. S. 293, 301 (1946) where this Court concluded: "The statutory policy of affording broad protection to investors is not to be thwarted by unrealistic and irrelevant formulae."

The language of the Act is clear. Just as there is no need to restrict its language by purportedly applicable common law rules of construction, *Securities & Exchange Commission v. Joiner Leasing Corporation*, 320 U. S. 344 (1943), there is no reason for resorting to local state law to determine whether a bank is a disposer of securities for value.

This Court should not permit the salutary effect of the civil remedy under the Securities Act to be diminished. The public benefit resulting from the Act is not to be measured merely by statistics as to the cases which appear in the reports. *Cf.* COMMENT, CIVIL LIABILITY UNDER THE FEDERAL SECURITIES ACT (1940) 50 Yale L. J. 90, 106, where the writer concludes: "Final judgment must wait upon high court decisions of the more important points of controversy; it is to be hoped that a countervailing liberalism will prevent the civil remedies from becoming merely an impotent symbol of Congressional regard for the rights of investors." The significance of the remedy is also manifested by the many controversies settled out of court.

Even more important than the disposition of controversies, is the course of conduct resulting from an appreciation of the availability of the remedy. Let this Court say that banks are no different from any other legal entities in their duty to make full and fair disclosure in transactions involving the use of the mails or interstate commerce and it will follow without serious question that banking institutions will direct a review of their procedures to make sure that none of their practices mislead the public.

2. The decision of the court below conflicts in principle with the decision of the Court of Appeals of the First Circuit in *Cady v. Murphy,* 113 F. 2d 988 (CA 1, 1940) *cert. den.* 311 U. S. 705. The conflict is stated to be in principle rather than an actual conflict because of the possible distinction, upon which the court below relied, between a broker and a bank.

The point that an agent, participating in the disposition of securities for value, is a seller seemed to be settled law, with the possible qualification that this would not apply to a purely mechanical forwarder, see Loss, Securities Regulations (1951) 341. The court below recognized that even a bare collecting agent is not a purely mechanical forwarder. Yet, it disregarded not only that point in deciding that the Act was not applicable, but also disregarded the very substantial personal interests which the defendant had in the collateral which was spurious. The conclusion of the court below that the Pennsylvania categorization of a collecting bank as an agent, even if correct, does not support the point that the defendant was not a seller within the federal law.

The question of liability must be distinguished from the question of applicability. A bare agent may not be liable under the Act, because he has made no statement but has merely carried out the disposition of the security for value. In such case he would properly be a seller under the Act, but he would have no liability. Where, however, as in this case, the agent, if the bank be deemed only such, has not only substantially participated in the disposition for value, but has made misleading and untrue statements, there is both applicability and liability under the Act.

If this Court grants the writ of certiorari, it will have the opportunity to resolve the difference in principle which now exists in the federal courts as to the applicability of the civil remedy under the Securities Act to an agent of a seller.

3. The question as to the available defenses for misleading and untrue statements is an important question of federal law which has not, but should be, settled by this Court. The Congressional history of the Act makes strikingly clear that the burden of defense for an improper statement is on the defendant, and interestingly shows the applicability of this rule to banks as well as to other businesses (H. R. 85, 73rd Cong., 1st S. 9-10, Cong. Doc. 9774):

> "Unless responsibility is to involve merely paper liability, it is necessary to throw the burden of disproving responsibility for reprehensible acts of omission or commission on those who purport to issue statements for the public's reliance. The responsibility imposed is no more nor less than that of a trust. It is a responsibility that no honest banker and no honest businessman should seek to avoid or fear."

The defense spelled out in the Act is very clear; i.e., the defendant must prove that it "did not know, and in the exercise of reasonable care could not have known of such untruth or omission . . ." The court below gave lip service to the rule by stating it but then proceeded to recognize two entirely different defenses.[3] One defense was an alleged warning given by the last sentence of a letter. Even a real warning is not a "saving grace" to a half-truth, nor is it a defense countenanced by the language and the basic principles of the Act. *Cf. Cady v. Murphy,* 113 F. 2d 988 (CA 1, 1940) *cert. den.* 311 U. S. 705 which recognized that contributory negligence is not a defense under the Act.

The other defense relied on by the Court of Appeals which permitted the defendant to escape liability for its untrue statement that it held warehouse receipts of the Carrollton Springs Pure Rye Distillery, Inc., was that the defendant was not a warrantor and had no duty to inves-

3. The District Judge did not pass on this issue. He concluded that the plaintiff had no cause of action under the Securities Act because the defendant was not a seller, and then he turned to questions of common law right of recovery.

tigate the documents.[4] This error of the Court of Appeals resulted from its failure to acknowledge that the duty comes into existence by virtue of the Act itself, which calls for a full and fair disclosure when any material statement is made. The whole liberal purpose of the Act will be seriously impaired if courts are going to look at common law conceptions of duties in measuring liability under the Act. No argument is made at this time with respect to what is believed to be an erroneous viewpoint by the courts below of the nature of the defendant's duty as it existed at common law because this request for certiorari is not based on that error. It is rather based on the importance of not permitting the public benefits of the civil remedy under the Securities Act to be whittled away by any common law conceptions of warranty and duty.

CONCLUSION.

In two important respects the court below has decided important questions of federal law which should be resolved by this Court. There is also a conflict in principle in decisions of two Courts of Appeal on a matter of substantial importance in making effective against agents the protective provisions of the Securities Act by way of civil remedy. Consequently, the petition for a writ of certiorari should be granted.

Respectfully submitted,

ISRAEL PACKEL,
Attorney for the Petitioner.

August 13, 1954.

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4. The Court of Appeals acknowledged that if a duty existed, it was violated (App. 9a): "If Fidelity had a duty to investigate the genuineness of these documents, quite obviously it did not fulfill that duty. Likewise it did not use reasonable care to fulfill this duty, if it existed, because a small amount of inquiry would have revealed whether the distillery had the officers whose names appeared on the notes and receipts and also whether the receipt in fact had been issued by the warehouseman. No such inquiry was made."

Appendix.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT.

No. 11,238

THE FIRST TRUST AND SAVINGS BANK OF ZANESVILLE, OHIO,
Appellant

v.

FIDELITY-PHILADELPHIA TRUST COMPANY

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

Argued April 6, 1954

Before GOODRICH, KALODNER and HASTIE, *Circuit Judges.*

OPINION OF THE COURT

(Filed June 28, 1954)

By GOODRICH, *Circuit Judge.*

This case presents the often recurring situation of two people who, doing business in the ordinary course, have been fooled by a swindler. The swindler disappears or goes to jail. Which of the two parties is to bear the loss his rascality has occasioned?

The trial court made very full findings of fact on the history of the dealings among the parties and also the facts of the immediate transactions out of which this suit arose. Those extensive findings need not be repeated here. See 112 F. Supp. 761 (E.D. Pa. 1953).

Our set of operative facts gets down to this comparatively simple case. A bank's customer (the bank being the defendant, Fidelity-Philadelphia Trust Company) brings to the bank what purports to be the negotiable promissory note of a whisky distiller. This note is accompanied by what purports to be a negotiable warehouse receipt evidencing a deposit of whisky, which is to be collateral security for the note. Both the note and the warehouse receipt are, in fact, spurious. The customer (Philadelphia Acceptance Corporation, hereafter called PAC) does two things. First, it deposits with the bank in its trust department the purported warehouse receipt, for which the bank issues a safekeeping receipt and puts the document in a file. This is a bailment for the benefit of PAC and the purchaser of the promissory note. The charge made by Fidelity for the service is barely sufficient to cover its expenses in connection therewith. Second, the customer, PAC, leaves with the collection department of the bank a draft drawn by itself in its own favor on the plaintiff, The First Trust and Savings Bank of Zanesville, Ohio, (Zanesville), which is to be the purchaser of the note. Forthwith defendant Fidelity credits its customer with the amount of the draft and charges PAC interest until the transaction is closed. It is closed by Fidelity's forwarding the draft, note and safekeeping receipt to Zanesville. This bank in turn sends Fidelity a check payable to Fidelity's order and drawn on the Chase Bank in New York. In due course of time this check clears and Fidelity is thus reimbursed for the credit it has made to its customer.

The first problem is: Does this transaction make Fidelity a seller within the terms of the Securities Act of 1933?[1] It should be noted that what was done here is very

1 "Any person who—

"(1) sells a security in violation of section 77e of this title, or

"(2) sells a security (whether or not exempted by the provisions of section 77c of this title, other than paragraph (2) of subsection (a) of section 77c of this title), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by

similar to what goes on in thousands and thousands of cases where a bank advances funds to its customer upon having endorsed to it the customer's draft on a third party, accompanied by a negotiable bill of lading or warehouse receipt. The only addition here is the keeping of the purported warehouse receipt in the files of Fidelity, not because Fidelity wanted it, but because of the arrangement made between PAC and Zanesville.[2] The situation differs also from the sight-draft-bill-of-lading-attached transaction in that here PAC's draft was accompanied by the distilling company's note, which was the supposed thing of value given for the loan.

If this set of facts constitutes Fidelity a seller under the Securities Act, it seems to us inevitable that every bank which advances money to a customer upon a sight draft and negotiable bill of lading is also a seller. True there are one or two additional facts in this case. Fidelity here stored in its safekeeping files the purported warehouse receipt. But we do not see that this fact affects the relation of the parties to the collection transaction. The deposit of the receipt was a convenience to PAC and Zanesville, for it made easier the substitution of new receipts and notes when this was in order. It was frequently in order, for during the years 1939 to 1950, Zanesville had made 220 purchases of distillers' notes fom PAC. The plan for such deposit with

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means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less than the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security." 15 U.S.C.A. § 77*l*.

2 Originally, PAC would forward the warehouse receipts directly to Zanesville. Because of the paper work required by this arrangement, a Zanesville teller asked PAC's agent to suggest a less cumbersome method of handling the receipts. He suggested that PAC deposit the receipts with defendant, which in turn would forward to plaintiff a safekeeping receipt, usually covering several warehouse receipts. Zanesville agreed to this procedure.

Fidelity was worked out by PAC and Zanesville, as shown in the recital in footnote 2.

It is also true that Fidelity sent some information to Zanesville at one time about its customer, PAC, at Zanesville's request. We do not see how that adds anything to the concept of Fidelity as a seller. The information was gratuitously given. Fidelity did not urge by intimation or express statement that Zanesville should act upon the information. Whether the letter had other legal consequence we shall discuss later.

The words of the federal Securities Act of 1933 are very, very comprehensive indeed. The subject matter includes documents such as drafts and notes. By express wording "sale" is pretty broadly defined. Here is the language: "The term 'sale', 'sell', 'offer to sell', or 'offer for sale', shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value . . ." 15 U.S.C.A. § 77b(3).

Furthermore, it can hardly be denied that when a bank takes a document for collection, advancing to its customer credit prior to the actual collection being made, the bank then becomes at least a security owner. Maryland Casualty Co. v. National Bank of Germantown, 320 Pa. 129, 182 Atl. 362 (1936). And see Note, 22 A.L.R. 2d 479 (1952). And when it endorses the instrument, on which it thus advanced credit, to another bank by the general endorsement "pay any bank, banker or trust company," and gets its money, has it not passed its interest in that document along to him who pays the draft and gets the supposedly valuable bill of lading, warehouse receipt or note accompanying the draft? And if that is so, why have we not been pushed into the startling conclusion that every bank that makes an advance on an instrument left with it for collection, and passes that instrument on to someone else, has become a seller under the terms of the federal statute, if the transaction is one in interstate commerce?

We think that we do not need to reach this startling conclusion, at least on the facts of this case. In this we are supported by the clearly established law of Pennsylvania with regard to the relation of a bank and its depositor. It is true that in construing the federal statute we are not, of course, bound by state law concepts. But in deciding whether Fidelity has done things which bring it under the terms of a federal statute, we look to the law of Pennsylvania to see the state law consequence of business dealings between PAC, a Philadelphia customer, and Fidelity, a Philadelphia bank.

In the case of each of the worthless notes involved in this litigation, PAC, as stated above, had drawn a draft in its own favor upon Zanesville. These drafts were endorsed to the order of Fidelity, without qualification. Such endorsement is a special endorsement under section 34 of the N.I.L.[3] and is in no sense a restrictive endorsement. Ordinarily when a person is given physical possession of a negotiable instrument thus specially endorsed to him he becomes the owner. But in Pennsylvania this matter is expressly covered by a statute of 1931 and that statute is important enough to quote here:

> "Except as otherwise provided by agreement and except as to subsequent holders of a negotiable instrument payable to bearer or indorsed specially or in blank, where an item is deposited or received for collection, the bank of deposit shall be agent of the depositor for its collection and each subsequent collecting bank shall be subagent of the depositor but shall be authorized to follow the instructions of its immediate forwarding bank, and any credit given by any such agent or subagent bank therefor shall be revocable until such time as the proceeds are received in actual money or an unconditional credit given on the books

3 Pa. Stat. Ann. tit. 56, § 85 (Purdon 1930); to be superseded by the Uniform Commercial Code, effective July 1, 1954.

> of another bank, which such agent has requested or accepted. Where any such bank allows any revocable credit for an item to be withdrawn, such agency relation shall, nevertheless, continue, except the bank shall have all the rights of an owner thereof against prior and subsequent parties to the extent of the amount withdrawn . . . " Pa. Stat. Ann. tit. 7, § 213 (Purdon 1939).

A later section of the same statute provides:

> "Where a deposited item is payable to bearer or indorsed by the depositor in blank or by special indorsement, the fact that such item is so payable or indorsed shall not change the relation of agent of the bank of deposit to the depositor, but subsequent holders shall have the right to rely on the presumption that the bank of deposit is the owner of the item . . . " Pa. Stat. Ann. tit. 7, § 215 (Purdon 1939).[4]

Now it is true that to become a "seller" under the Securities Act one does not have to be the owner of that which he "sells." A broker can, under some circumstances, become a "seller." Cady v. Murphy, 113 F. 2d 988 (C.A. 1), cert. denied, 311 U.S. 705 (1940) (seller's broker); Boehm v. Granger, 181 Misc. 680, 42 N.Y.S. 2d 246 (Sup. Ct. 1943), aff'd without opinion, 268 App. Div. 855, 50 N.Y.S. 2d 845 (1st Dep't 1944) (buyer's broker). On the other hand, Professor Loss says that there are various kinds of mechanical activities which do not come

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4 These two sections will be superseded by the Uniform Commercial Code, which becomes effective July 1, 1954 in Pennsylvania. The Code provision reads as follows:

"Unless a contrary intent clearly appears, a depositary bank takes an item for collection regardless of the form of indorsement or lack of indorsement and even though credit for the item is subject to immediate withdrawal as of right." Pa. Stat. Ann. tit. 12A, § 4-201 (Purdon 1954).

See also the comment to that section. The rule likewise represents the case law in Pennsylvania. See Lipschutz v. Phila. Savings Fund Soc., 107 Pa. Super. 481, 164 Atl. 74 (1933), and cases cited therein; Foster v. Federal Reserve Bank of Phila., 29 F. Supp. 716 (E.D. Pa. 1939), aff'd, 113 F. 2d 326 (C.A. 3, 1940).

under the statute and his extensive experience in this field gives his view importance, especially in the absence of case law to the contrary.[5]

The agent for collection under the Pennsylvania law is not a purely "mechanical" forwarder. He is not a seller. Nor is he a broker. But we think that the clear and insistent characterizing of the collecting bank under Pennsylvania law as agent supports our conclusion that Fidelity in receiving drafts from PAC and forwarding them for collection to Zanesville did not become a seller under the Federal Securities Act.

Assume now that what is said above is incorrect, and that we are driven to the conclusion that Fidelity was a "seller," under the Securities Act. What has it done which will place liability upon it? Or, to put the matter in a different way, in statutory language, has it met the burden the statute places on it to prove that, if there was an untruth or omission, it "did not know, and in the exercise of reasonable care could not have known of such untruth or omission . . ."[6] There are two points in this connection made by Zanesville.

One of the points has to do with a letter which the credit manager of Fidelity sent to Zanesville back in March, 1949.[7] That letter was in answer to an inquiry made of Fidelity by Zanesville concerning the credit of Philadelphia Acceptance Corporation, which was a customer of Fidelity for other things than the kind of transaction described above. Fidelity's answer started by announcing in big type that the information was gratuitous and given as a business courtesy.[8] We make nothing of that. A man may become just as much liable for the consequences of his lie

5 Loss, Securities Regulation 341 (1951).

6 See note 1, supra.

7 The transactions out of which the spurious notes and warehouse receipts arose were consummated in July, 1950.

8 "This information is furnished as a matter of business courtesy on the understanding it is confidential and no responsibility therefor attaches to this bank or any of its representatives."

if he does it for nothing as if he gets paid for it. Restatement, Torts § 552, comment *c*.

Appellant makes much of the point that the financial affairs of Mr. Collom, the president and perhaps sole shareholder of PAC, were not mentioned in Fidelity's letter. We make nothing of this either. The inquiry was about the corporation. Furthermore, we do not know whether tax liens which are said to have existed against Mr. Collom at the time were or were not subsequently satisfied. Nor do we know about a judgment which was said to be outstanding against him at the time—whether it was reversed, satisfied or what. At any rate, the inquiry was about the corporation and it was the corporation which was Fidelity's customer.

There is more to be said about the letter however. It went on to say that PAC's account was handled in a satisfactory way and gave an explicit statement about an average five-figure balance. This five-figure statement was true but it was also found as a fact that twelve times in the two months before the letter was written, PAC had had overdrafts amounting to sums from several hundred dollars to over thirty-six thousand dollars. We do not go with the argument that when a man says something that is literally true he has told the truth even though he does not tell the other things which would qualify the statment made. "To tell half a truth only is to conceal the other half."[9] But the saving grace of the letter is the last sentence. The defendant's credit manager said: "A condensed balance sheet exhibited to us last year indicates that the net worth of the Philadelphia Acceptance Corporation is limited and is substantially less than outstanding obligations." That, we think, is enough. The sum total impression from the letter is truthful and certainly gives warning to one who is

9 Mitchell, J., in Newell v. Randall, 32 Minn. 172, 173 (1884). Restatement, Torts § 529: "A statement in a business transaction which, while stating the truth so far as it goes, the maker knows or believes to be materially misleading because of his failure to state qualifying matter is a fraudulent misrepresentation."

prospectively going to extend credit to the concern inquired about.

The other incorrect representation alleged to have been made by Fidelity is the statement on the safekeeping receipt that such and such warehouse receipts had been received and placed in the safekeeping file. If Fidelity had a duty to investigate the genuineness of these documents, quite obviously it did not fulfill that duty. Likewise it did not use reasonable care to fulfill this duty, if it existed, because a small amount of inquiry would have revealed whether the distillery had the officers whose names appeared on the notes and receipts and also whether the receipt in fact had been issued by the warehouseman. No such inquiry was made. It is also true that Zanesville could have found out with equal ease and convenience, or at least almost equal ease and convenience, about the genuineness of the documents. So our question becomes: Does a bank, when it takes a document for its safekeeping file for a customer and issues a receipt describing the document, warrant or have a duty to find out about the genuineness thereof?

It would be somewhat surprising to find an affirmative answer to this question. As noted above, Fidelity made but a nominal charge for this safekeeping facility and that nominal charge hardly covered its expenses. It quite obviously was not voluntarily getting itself into a position of warranting the genuineness of documents left with it for safekeeping. An analogy to this situation can be found in letter of credit cases. A bank which pays in good faith against a forged bill of lading can recover from the customer for whom it issued the letter. The bank is under no duty to investigate the genuineness of the shipping document. A leading case is Brown v. Rosenstein, 120 Misc. 787, 200 N.Y. Supp. 491 (Sup. Ct. 1923), aff'd without opinion, 208 App. Div. 799, 203 N.Y. Supp. 922 (1st Dep't 1924). See McCurdy, Commercial Letters of Credit, 35 Harv. L. Rev. 715, 734-735 (1922); and Ward and Har-

field, Bank Credits and Acceptances 54-55, 93-98 (3d ed. 1948).

We have another analogy in warehouse cases. In Dean v. Driggs, 137 N.Y. 274, 33 N.E. 326 (1893), a warehouseman gave a receipt for "fifteen hundred barrels Portland cement." The court held the warehouseman not liable to the endorsee of the receipts because the barrels contained a worthless substance. Judge Peckham said: "In its very nature it seems to me plain that no warranty as to contents can reasonably be implied under these circumstances from the use of such language as these receipts contain." 137 N.Y. at 282, 33 N.E. at 328. See also Hale v. Milwaukee Dock Co., 23 Wis. 276 (1878). Later cases of this sort are lacking because of the custom of inserting language such as "said to contain" and "contents unknown" in documents of title. See 2 Williston on Sales 582-583 (Rev. ed. 1948).

We think this is right. We cannot think that either the giver of such a receipt as Fidelity issued here or the person who gets it expects the bailee for safekeeping to warrant the genuineness of the warehouse receipts or to stir about and investigate their validity. It would be easy enough for the issuer of such a receipt to make it read in terms of "documents purporting to be warehouse receipts for whisky and bearing what purports to be the signatures of certain officers," but we do not think that documents issued by the thousands in everyday business, as such things as these must be, must hedge every statement made with the supercaution of a corporate mortgage. Fidelity is not liable either as a warrantor nor as one who had a duty to investigate and failed to perform it.[10]

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10 Note that the Uniform Commercial Code specifically limits the warranties of a collecting bank as to documents: "A collecting bank or other intermediary known to be entrusted with documents on behalf of another or with collection of a draft or other claim against delivery of documents warrants by such delivery of the documents only its own good faith and authority. This rule applies even though the intermediary has purchased or made advances against the claim or draft to be collected." Pa. Stat. Ann. tit. 12A, §7-508 (Purdon 1954).

The above discussion covers both the liability of the defendant as a "seller" under the Securities Act and also, we think, common law liability in the nature of deceit or for negligence in the use of language.

There is also a point made concerning the reference to collateral in the drafts drawn by PAC upon Zanesville. For instance, the draft of July 21, 1950, for $19,000, after the usual date, direction to pay, amount, name of drawee, and so on has this clause: "$19,000 ALEXANDER YOUNG DISTILLING Co. Collateral Note No. SY-274 dated 7/21/50—due 8/7/50, together with Fidelity-Philadelphia Trust Co. Safekeeping Receipt covering the collateral as fully described on the face of the note." Does that reference make the endorser (that is, Fidelity) a guarantor of the genuineness either of the note or the warehouse receipts which are collateral for the note? This question was raised and decided clearly in the negative in Hubbard Bros. & Co. v. Southern Pac. Co., 256 Fed. 761 (C.A. 5, 1919). To the same effect is the King's Bench decision in Guaranty Trust Company of New York v. Hannay & Co., [1918] 2 K.B. 623. See also, discussing the problem, Note, 32 Harv. L. Rev. 560 (1919). We agree with those decisions.

What has been said takes care, either directly or by necessary inference, of the case made by the plaintiff. It has been thoroughly and competently presented for both sides, but we think the defendant should win and that the decision of the lower court was right.

The judgment of the district court will be affirmed.

JUDGMENT.

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby affirmed, with costs.

Attest:

IDA O. CRESKOFF,
Clerk.

June 28, 1954

In the Supreme Court of the United States

October Term, 1954.

No. 292.

The First Trust and Savings Bank of Zanesville, Ohio,
Petitioner,

v.

Fidelity-Philadelphia Trust Company,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit.

BRIEF FOR RESPONDENT IN OPPOSITION.

The Court of Appeals for the Third Circuit unanimously affirmed a judgment of the United States District Court for the Eastern District of Pennsylvania in favor of the respondent bank in a suit by the petitioner bank based in part on a claimed violation by the respondent of Section 12(2) of the Securities Act of 1933. That Section imposes liability upon a person who in the use of interstate commerce or the mails sells a security by means of a prospectus or oral communication which includes an untrue statement of or omits a material fact, and who fails to sustain the burden of proof that he did not know and in the exercise of reasonable care could not have known of the untrue statement or omission.

The suit grew out of the petitioner bank's purchase

of four purported notes of whisky distillers, secured by spurious whisky warehouse certificates, from Philadelphia Acceptance Corporation ("PAC") in July, 1950. PAC was a depositor in the respondent bank and had been engaged for many years in selling whisky distillers' collateral notes to the petitioner and other banks. The history of the dealings among the parties and the facts of the immediate transactions out of which the suit arose were the subject of very full findings of fact by the District Court, which, in addition to holding that respondent did not sell the notes and had not been under any duty to investigate the validity of the notes or warehouse certificates, found that respondent had made no misrepresentations and had not been negligent. The Court of Appeals agreed.

OPINIONS BELOW.

The opinion of the District Court (R. 205a-228a)[1] is reported at 112 F. Supp. 761.[2] The unanimous opinion of affirmance by the Court of Appeals (App. 1a-11a) is reported at 214 F. 2d 320.

JURISDICTION.

The judgment of the Court of Appeals was entered on June 28, 1954 (App. 12a). A petition for rehearing was filed by petitioner on July 12, 1954 and denied by the Court of Appeals on July 20, 1954. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

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[1] "R." followed by page citation refers herein, as in the petition, to pages of the printed appendices to the briefs of both parties in the Court of Appeals, where the appendix to the brief for the appellant constituted pages 1a to 231a, and the appendix to the brief for the appellee constituted pages 232a to 442a. "App." refers herein, as in the petition, to the appendix to the petition itself.

[2] An earlier memorandum opinion of the District Court in this and certain related cases, on defendant's motions for more definite statements and to strike portions of the complaints, is reported at 12 F. R. D. 195.

QUESTIONS PRESENTED.

1. Did the respondent bank "sell" securities to the petitioner bank within the meaning of the Securities Act of 1933, where one of respondent's depositors, after contracting to sell a whisky distiller's collateral note to the petitioner, would deposit a draft in the respondent bank drawn on petitioner for the purchase price, with the note attached, and respondent would revocably credit the depositor's account with the amount of the draft, forward it with the note to the petitioner, collect the amount of the draft, and charge the depositor with interest for the period of collection?

2. Did respondent make untrue statements or omissions of material fact in (*a*) its safekeeping receipts for whisky warehouse certificates left with it in safekeeping by its depositor for the account of the petitioner, as collateral for the notes, under arrangements made between the depositor and the petitioner, or in (*b*) a letter concerning the depositor's financial standing, written fifteen months before petitioner's purchase of the notes in question, wherein respondent informed petitioner as to the depositor's average balances and advised petitioner that the depositor's net worth was substantially less than its outstanding obligations, but did not also specifically mention a number of temporary overdrafts that had occurred in the depositor's account?

3. Did respondent exercise reasonable care under the circumstances in not investigating the genuineness of the whisky warehouse certificate collateral which it held in safekeeping for the petitioner under arrangements made between petitioner and respondent's depositor?

STATUTE INVOLVED.

Section 12(2) of the Securities Act of 1933 (Act of May 27, 1933, Ch. 38, 48 Stat. 74), 15 U. S. C. Section 77*l*(2), reads as follows:

"Any person who——

* * * * * * *

sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (*a*) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes *an untrue statement of a material fact or omits to state a material fact* necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of *reasonable care* could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security." (Emphasis added.)

Section 2(3) of the Act, 15 U. S. C. Section 77b(3), defines "sell" as follows:

"(3) the term 'sale', 'sell', 'offer to sell', or 'offer for sale' shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value; * * *."

STATEMENT.

In the summer of 1950 PAC sold to petitioner and other banks which had long been its customers a number of forged or otherwise worthless whisky distillers' notes secured by forged warehouse certificates deposited by PAC with the respondent bank in safekeeping for the account of the purchasing banks as collateral for the notes. Respondent itself was defrauded by PAC on loans of some $300,000 which it had made to PAC on the security of similarly spurious collateral (R. 213a). As a result of the fraud PAC's president went to jail (R. 214a).

At the time of its purchase in July, 1950 of the four notes involved in this suit the petitioner had already been buying distillers' collateral notes from PAC since 1939, or for more than eleven years (R. 205a). Over that period of time petitioner had purchased from PAC a total of approximately 220 distillers' notes, in an aggregate face amount of more than $3,000,000, secured by whisky warehouse certificates and carrying an interest yield to petitioner of as high as five percent (R. 45a, 205a; Exh. D5, R. 391a-396a, 175a).

The District Court found that the general course of conduct in all such purchases by petitioner was that the notes would first be offered to petitioner directly by PAC via telephone, telegram or letter and that petitioner would accept or reject the offer by telephone communication directly with PAC (R. 205a). The District Court further found that this previously adopted system of offer and acceptance directly between PAC and petitioner was also followed in the case of the petitioner's purchase of the four notes here involved (R. 207a, 209a, 210a). And on the evidence the District Court firmly refused to recede from this finding, although petitioner pressed it to do so in a motion to amend the findings (R. 229a, 231a).

The District Court also found that after PAC would thus offer the petitioner a note and the petitioner would thus accept the offer by telephone, the physical mechanics of consummating the already agreed upon purchase were as follows:

PAC would send petitioner a check in payment of a prior note that was being replaced by the new note that petitioner had just agreed to purchase, at the same time also sending petitioner a written confirmation of the new sale, together with an independent appraisal of the market value of the whisky collateral (R. 208a).

On the same day PAC would deposit to its account with respondent a draft drawn by PAC on petitioner, to which was attached the new note that petitioner had agreed to buy (R. 207a). Respondent's Collection Department would stamp the draft with the respondent's collection endorsement, forward it to petitioner with the attached note and a safekeeping receipt (referred to below) for the collateral, and in a few days receive payment of the amount of the draft in accordance with PAC's instructions to petitioner (R. 207a, 208a). Upon the mailing of the note, draft and safekeeping receipt to petitioner, respondent in keeping with regular banking usage and custom in such cases would revocably credit PAC's checking account, and upon collection would reimburse itself from the proceeds and charge PAC with interest for the number of days required for the collection (R. 208a, 209a).

When depositing a draft with note attached in respondent's Collection Department, as above, PAC would also leave with respondent's Corporate Trust Department, for safekeeping for petitioner, the whisky warehouse certificate or certificates which constituted the collateral for the note involved in the particular transaction (R. 207a). Respondent's Corporate Trust Department would then prepare a safekeeping receipt for this collateral, reciting

therein that respondent had received of petitioner the collateral identified in the safekeeping receipt (R. 207a). As stated above, this safekeeping receipt went to the petitioner along with the draft and note.

The District Court also found that the safekeeping arrangement had been worked out directly between PAC and petitioner in 1942, as a convenience to the petitioner and as a consequence of its having complained to PAC concerning the trouble and expense involved in sending the warehouse certificate collateral back and forth between PAC and petitioner when a note was purchased or a different warehouse certificate was to be substituted for the initial collateral (R. 206a). As the District Court further found, respondent made no profit from its safekeeping, the charge which it received for this service being only enough to reimburse it for its out-of-pocket expense in connection with the clerical work involved (R. 207a).

Each distiller's note purchased by petitioner described the whisky warehouse certificate collateral behind it by serial number, the number of barrels and nature of the whisky therein, the date of the Government's original inspection for tax purposes, the geographical location of the Government's warehouse where the barrels were stored, the number of gallons of whisky, the name and address of the issuer of the warehouse certificate, and the maker of the note (R. 136a, 165a). The same information was repeated on respondent's safekeeping receipt, the information on which was taken from respondent's copy of the note and compared against the corresponding information on the warehouse certificate (R. 128a, 136a). The District Court found that this information afforded petitioner sufficient basis at any time it desired to check on the validity of the whisky certificates or the value of the security (R. 215a).

The District Court also found that not only did petitioner never request respondent to verify the validity of any note or warehouse certificate, but that in addition the warehouse certificates were apparently properly signed and in good order and form and that there was nothing on their face to put respondent on notice of possible fraud or invalidity (R. 214a). Significantly, petitioner did not detect similar forgeries in the notes themselves, which were in its own hands (117a, 118a). It was likewise found that petitioner was relying upon PAC's representations in dealing with that company (R. 214a).

It was further found by the District Court that the only direct communication between petitioner and respondent consisted of an exchange of letters in the middle of March, 1949 (R. 215a). On March 14 of that year petitioner wrote a letter to respondent asking for respondent's opinion as to PAC's financial responsibility (R. 215a). In its reply on March 17, 1949, which was sent simply as a business courtesy and on the express understanding that no responsibility therefor was to attach to respondent, respondent supplied petitioner with completely truthful information as to PAC's average balances and as to its condensed balance sheet, which, as respondent pointed out to petitioner, showed that PAC's net worth was limited and substantially less than its outstanding obligations (R. 216a, 217a).

The average balances of PAC for the then uncompleted month of March, 1949 were unavailable at the time of respondent's foregoing reply, and in its letter respondent did not attempt to refer at all to PAC's balances for that month. In the trial and appeal of this suit petitioner sought to capitalize on the circumstance that during the first half of that month PAC was temporarily overdrawn on a number of days in its checking account with respondent. However, the District Court found that respondent's letter was a truthful statement of the facts and not in any way misleading, either by misstatement

or omission to state material facts (R. 219a, 220a). It also found that nothing said or done by respondent constituted a misrepresentation or concealment of the facts (R. 220a). The Court of Appeals did not disturb the District Court's findings and particularly agreed that the impression from respondent's letter could not have been misleading under the circumstances (App. 8a, 9a).

After petitioners' purchase in July, 1950 of the four notes involved in this suit it was discovered that PAC had been guilty of fraud upon purchasers of distillers' notes by forging some of the notes and whisky warehouse certificate collateral (R. 212a, 213a). It was ascertained that among others the warehouse certificates for the four notes here involved, as well as three of these notes themselves, were forgeries (R. 117a, 213a). However, the District Court found that respondent had no intimation of PAC's fraud prior to its discovery (212a, 213a, 219a).

PAC having gone into bankruptcy, petitioner and a number of the other banks which had been defrauded by PAC brought suits against respondent in the District Court below. Petitioner's suit, seeking to recover $82,000 as the aggregate face amount of the four notes, plus interest and costs, asserted diversity of citizenship between the parties and alleged violation of common law obligations and various statutes, including the Securities Act of 1933.

Trial in the District Court was without a jury in January, 1953 and lasted several days. The evidence consisted of oral testimony and more than eighty exhibits, with considerable evidence as to customary banking procedure and usage.

The District Court filed its opinion and findings and entered judgment for defendant on May 28, 1953 (R. 206a-229a). Plaintiff's motions to amend the findings and judgment and for a new trial were filed on June 5, 1953 (R. 229a, 230a) and were denied on November 2, 1953 (R. 231a). Appeal to the Court of Appeals was taken on

November 30, 1953. It was argued on April 6, 1954 and judgment was affirmed on June 28, 1954 (App. 1a-12a). Appellant's petition for rehearing was denied on July 20, 1954 and was followed by the present petition, filed August 18, 1954.

ARGUMENT.

As reasons for granting the writ petitioner contends that the case involves important questions of federal law which have not been, but should be, settled by this Court, and that the decision of the court below conflicts in principle with a decision from another Circuit. As will be shown, these contentions are without merit. It is also submitted that the result reached in the court below was clearly correct.

I.

No Important Question of Federal Law is Involved.

A. Petitioner first urges that the determination of "whether a restricted interpretation should be given to the word 'seller' under the Securities Act is an important question of federal law which has not been, but should be, settled by this Court," and that great public significance exists in the intertwined issue of "whether banks, in the performance of banking operations, can be sellers within the meaning of the Act" (Pet. 7). No such vague and general question is presented by this case.

The petition would make it appear that the court below issued some sort of a sweeping pronouncement to the effect that the word "sell" in the Securities Act can never apply to banking institutions or their operations. Actually the court below made it perfectly clear that its decision was not grounded upon such a concept but, on the contrary, was based upon the special and unique facts of this particular case.

Thus, at the outset of its discussion of the Securities Act the Court of Appeals made plain its full recognition that the words of the Act are quite comprehensive and that the word "sale" is broadly defined therein (App. 4a). It is true that the court also, and very properly, raised a query as to whether the line of argument advanced by petitioner would not result in the startling conclusion that every bank which makes an advance on an instrument left with it for collection and passes the instrument on to someone else becomes a seller under the Act, if the transaction is in interstate commerce. However, the court then went on to state explicitly that it did not need to reach this startling conclusion, "at least on the facts of this case" (App. 5a).

It is entirely evident from the opinion of the Court of Appeals, whether read in part or in whole, that the court was not attempting to lay down any general rule of non-liability of banking institutions under the Securities Act, but was predicating its decision upon the particular facts of the case at hand. Those facts, it pointed out, had been made the subject of very full and extensive findings by the District Court (App. 1a). Indeed, the District Court's findings of fact, tracing the special nature and lengthy history of the arrangements and relationships of the parties, take up more than fifteen printed pages of the Record (R. 205a-220a) and establish that PAC, not respondent, was the disposer of the notes for value and therefore the seller within the meaning of the Act.

Petitioner complains (Pet. 7, 8) because the Court of Appeals, in holding that under the facts of this case respondent did not sell the notes to the petitioner within the meaning of the Securities Act, noted that it was *supported* in this conclusion by the clearly established law of Pennsylvania, as codified there by statute, with regard to the agency relation between a bank and its depositor. The court, however, fully recognized that the

local law simply supported its decision, without being in any way conclusive thereon, since "in construing the federal statute we are not, of course, bound by state law concepts" (App. 5a). Furthermore, in adverting to the Pennsylvania statute the court was doing no more than answering the petitioner's own contention that when respondent gave PAC a revocable credit for the amount of a draft deposited with it by PAC for collection, respondent became owner of the note and collateral.

Moreover, the assertedly important question as to the meaning of the word "seller" under the Securities Act was not even essential to the decision in this case, as the court below took pains to observe, since the judgment in respondent's favor was also reached on alternative grounds. The present case, therefore, is not one which would afford a desirable vehicle for review of the broad issue that petitioner attempts to raise.

B. It is also urged by petitioner that the question "as to the available defenses for misleading and untrue statements is an important question of federal law which has not, but should be, settled by this Court" (Pet. 10). That vague and abstract question, however, is likewise not presented by the case, since the respondent did not make a misleading or untrue statement. This was one of the District Court's express findings (R. 219a, 220a), and the Court of Appeals saw fit not to disturb it.

Petitioner had claimed two misleading or untrue statements by respondent. One of these consisted of respondent's letter of March 17, 1949, relating to PAC's financial standing. As to this letter, which was written more than fifteen months before petitioner purchased the notes here involved, the District Court found that the information therein was truthful and not misleading, either by way of misstatement or omission (R. 219a, 220a). The Court of Appeals agreed that the letter was completely truthful in the sum total impression which it gave (App. 8a).

The other claimed misleading statement by respondent was the language in its safekeeping receipts, which recited that respondent had received of petitioner the warehouse certificate collateral described therein and which then went on to identify the warehouse certificates by the descriptive information appearing on the face thereof (*i. e.*, the certificate serial number, the serial numbers and quantity of the barrels, the location of the warehouses, etc.). With respect to these safekeeping receipts the District Court found that nothing said or done by respondent in any of the transactions in suit constituted a misrepresentation or concealment of facts (R. 220a). The Court of Appeals likewise recognized that under no reasonable construction of the safekeeping receipts could they be interpreted as constituting a statement or representation by respondent that it had received genuine warehouse receipts. This the Court of Appeals made clear by pointing out that although the safekeeping receipts of course could have been phrased so as to describe the safekept documents as "purporting to be" warehouse certificates and as bearing what "purports to be" the signatures of certain officers, there was no need whatever for such supercautionary language in documents issued by the thousands in everyday business, as such things as these must be (App. 10a).

In finding that respondent's safekeeping receipts were not misleading under the circumstances, both the District Court and the Court of Appeals very properly took into consideration that respondent was under no duty to investigate the validity of the warehouse certificates, in view of the relationship of the parties and the other facts of the case. The absence of this duty made it all the more evident that the safekeeping receipts were not reasonably construable as statements or representations by respondent that the warehouse certificates were genuine. The petition, however, being based on the erroneous assumption that the safekeeping receipts were misstatements as to the genuineness of the certificates, proceeds in turn to torture

the conclusion of the Court of Appeals, as to the absence of a duty to investigate, into a claimed departure from the defenses available under the Securities Act. Petitioner's misconception of the nature of the court's holding on the point provides its own answer to this part of the petition.

II.

There Is No Conflict in Decision or Principle.

The other reason assigned in the petition for granting the writ (Pet. 9) is an asserted conflict in principle between the decision of the court below and that of the Circuit Court of Appeals for the First Circuit in *Cady* v. *Murphy*, 113 F. 2d 988 (1940), cert. den. 311 U. S. 705 (1940). Petitioner's contention on this point is equally without merit.

The *Cady* case simply involved the liability of one occupying a position comparable in the present case to that of PAC, not respondent. In *Cady* the defendants were a brokerage firm (Rhoades & Company), which had both negotiated and effected the sale through its head trader, one Lynch, by means of his misrepresentation of material facts. They were the sellers in every sense of the word. The completely different situation there, as compared with the one here, is reflected in the following summary of the facts by the Circuit Court of Appeals in that case (113 F. 2d at pages 989-990):

> "The plaintiff is a small securities broker and dealer doing business in Portland, Maine, under the name of Clifford J. Murphy Co. For many years he had extensive dealings with the defendants, a firm of stock brokers carrying on a general brokerage business under the name of Rhoades & Company with offices in New York and Boston. *Negotiation of the transaction out of which the present lawsuit arose was conducted by Murphy and Frank Lynch, the head*

trader of Rhoades & Company, by means of numerous telephone conversations between Boston and Portland. Early in March, 1937, Lynch persuaded Murphy to purchase voting trust certificates representing 1,700 common shares of South American Utilities Corporation (incorporated in Delaware), part of a block of 1,970 shares which had been held by E. E. Smith & Company, a small unlisted dealer in New York. *The court below found that Lynch had effected the sale by misrepresentation of material facts, and further found that the defendants had not sustained the burden of proof that Lynch did not know, nor in the exercise of reasonable care could have known, of the untruth of the misrepresentations.* These findings are amply sustained by the testimony and indeed are not assailed by appellants." (Emphasis added.)

Respondent in the present case was not the seller or even a selling agent, as in *Cady,* but simply served as a bank collection agent and safekeeping depositary pursuant to arrangements therefor made directly between petitioner and PAC.

III.

The Decision Below Is Clearly Correct.

The District Court's judgment for respondent followed a full trial of the facts and a careful review of the law. The unanimous affirmance by the Court of Appeals came after a similarly careful study of both the facts and the law. It should also be noted that the decision in the defendant's favor was made to rest on alternative grounds. The result was correct under the Securities Act, as well as under the common law counts, for any one of several equally sound reasons, briefly listed below:

First, the respondent did not "sell" the securities to petitioner but merely lent its services to petitioner and PAC in the physical mechanics of consummating sales

upon which petitioner and PAC had already agreed by telephone before the respondent so much as entered the picture (R. 205a), as is further shown by PAC's written sale-confirmations to petitioner (R. 208a) and from the fact that when petitioner purchased a new note it would usually be in replacement of another note already held by it (R. 208a; Exh. A-1 to A-4, R. 238a-321a, 175a).

Second, even if respondent had been a seller of the notes within the meaning of the Securities Act, it did not make an untrue statement of a material fact or omit to state a material fact necessary in order to make its statements, in the light of the circumstances under which they were made, not misleading. Without again adverting to the findings of the District Court and the concurrence of the Court of Appeals in this connection, we may note additionally that in view of the District Court's finding (R. 214a) that petitioner was relying upon PAC (not upon respondent) in its dealing with PAC, the alleged misstatements or omissions on respondent's part could hardly have been "material". It is true that proof of reliance and causal connection between the alleged misstatement or omission and the purchase is not an express requirement of the Securities Act, but it has been observed that unless relied upon and causally connected with the loss, an alleged untruthful statement will not be material under the Act. *Shulman, Civil Liability and the Securities Act,* 43 Yale Law Journal 227, 249-251 (1933).

Third, even assuming that respondent sold the notes and even assuming it did so by means of a misstatement or omission of material fact, respondent still sustained any burden of proof resting upon it to show that it did not know, and in the exercise of reasonable care could not have known, of such untruth or omission. This is not only evident from the correct conclusion of the District Court (R. 227a) and the Court of Appeals (App. 10a) that in the exercise of reasonable care under the circumstances respondent had no duty to investigate the

validity of the warehouse certificates, but it is also manifest from the finding by the District Court that respondent acted under the circumstances of the case as a reasonably prudent bank and was not negligent either in handling the whisky warehouse certificates or in not attempting to investigate the validity of the notes or the existence of the whisky collateral (R. 220a). This finding was fully supported by the evidence, which showed that in the performance of services of the nature which respondent here carried out, it has never been the function of one occupying respondent's position in the transaction to check the validity of the documents.

On any or all of the foregoing grounds the result reached by the District Court and Court of Appeals was clearly correct.

CONCLUSION.

The decision below involves no important question of law nor any conflict of decision or principle, and it is clearly correct on any one of a number of alternative grounds. The petition for a writ of certiorari should be denied.

Respectfully submitted,

ARTHUR LITTLETON,
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J. WESLEY OLER,
Attorneys for Respondent.

September 15, 1954.